No. 17-494

In the Supreme Court of the United States

SOUTH DAKOTA,

Petitioner,

–v–

WAYFAIR, INC., OVERSTOCK.COM, INC., and NEWEGG, INC.,

Respondents.

On Writ of Certiorari to the Supreme Court of South Dakota

BRIEF OF AMICUS CURIAE NATIONAL AUCTIONEERS ASSOCIATION AND 38 STATE AUCTIONEER ASSOCIATIONS IN SUPPORT OF THE RESPONDENTS

JONATHAN M. DUNITZ
COUNSEL OF RECORD
DAVID E. WARREN
BRIAN T. MARSHALL
VERRILL DANA, LLP
ONE PORTLAND SQUARE
PORTLAND, ME 04101
(207) 774-4000
JDUNITZ@VERRILLDANA.COM

APRIL 4, 2018 *COUNSEL FOR AMICUS CURIAE*

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INTEREST OF AMICUS[1]

The National Auctioneers Association (NAA) is the world's largest association of auction professionals. The NAA is a membership-based organization representing nearly 4,000 auctioneers serving a wide range of individuals, businesses, and industries. The 38 state auctioneer associations[2] joining NAA in this brief represent even more auctioneers, some of whom are also members of the NAA. Members and non-members alike recognize the NAA and their state associations as the voice of all auctioneers when laws or regulations threaten their livelihood.

Auctioneering is one of the world's oldest professions. Although a majority of auction companies are small, often family-owned businesses, auctioneers collectively facilitate commerce in America on a massive scale, selling a diverse variety of goods via live, online, and simulcast (concurrent live and online) auctions. It is common for an auctioneer to sell a $100,000 John Deere tractor and a $10 yellow pie plate at the same estate auction on a Saturday morning and, that evening, sell a table full of cakes at a charity auction

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[1] Petitioner and Respondents have filed blanket consents to amicus briefs. Pursuant to Rule 37.6 no counsel for a party authored this brief in whole or in part, and no party or counsel for a party, or any person other than the amicus curiae or their counsel, made a monetary contribution to fund the preparation or submission of this brief.

[2] A full list of the state auctioneer associations is included in the Appendix.

to support someone who is receiving cancer treatment in their local community.

While the chant of the auctioneer is familiar to many, the scale of the work auctioneers do to convert assets to cash is underappreciated. Auctioneers sell billions of dollars of idle assets each year, putting those assets back to work, and providing a valuable service to businesses, governments, individuals, communities, and the larger economy.

Auctioneers do not typically own the goods they sell at auctions, serving instead as agents of the sellers. In this capacity, auctioneers handle the marketing and logistics of auctions. As agents, auctioneers collect and remit sales taxes on the sale of goods sold and delivered in the jurisdiction of the auction.

One cannot overstate the adverse impact on auctioneers if this Court overrules the precedent it adopted more than 50 years ago in *National Bellas Hess, Inc. v. Department of Revenue of Illinois*, 386 U.S. 753 (1967) and affirmed 25 years later in *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992). Auctioneers have relied on this rule to determine when to collect and remit sales taxes, and the certainty afforded by the physical presence rule has allowed the auction profession to evolve and embrace online and other forms of interstate sales. If this Court overturns the physical presence rule, auction companies will face a complex web of state and local sales tax collection obligations and may become subject to retroactive sales tax liability for prior sales. While large retailers may be able to meet the burden of complying with multiple state and local taxation regimes, many auction companies and other small businesses will simply not

have the resources to absorb the costs of such compliance. The NAA and state auctioneer associations, on behalf of their members, have a vital interest in the outcome of this case.

INTRODUCTION AND SUMMARY OF ARGUMENT

Petitioner and its Amici cast their effort as a noble attempt to correct the "wrong" *Quill* decision and allow states to require internet retailers to pay their "fair share" of state sales taxes while purportedly imposing a "negligible burden" on interstate commerce. The burden is not negligible for thousands of small and medium-sized businesses that have relied—and continue to rely—on *Quill* to conduct interstate sales. For these businesses, including NAA's members, eliminating *Quill*'s physical presence requirement is not immaterial. It is an existential threat.

Auction companies are typical of small businesses throughout the country, and like many small businesses auction companies operate in a highly regulated environment.[3] More than 94% of NAA's member companies have twenty or fewer staff members and more than 80% have fewer than ten total employees.[4] Businesses this size simply cannot

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[3] Many but not all states require that auctioneers be licensed to conduct auction sales in those states, while in other states licensure is required at the county or municipal level.

[4] National Auctioneers Association, Membership Database (March 12, 2018).

afford to hire tax compliance professionals or spend hours of staff time identifying, collecting, and remitting sales taxes in thousands of different taxing jurisdictions.

Petitioner argues that tax compliance software provides real time compliance support for little to no cost. Minimal investigation reveals that this sales pitch is vastly overstated. As one provider of tax compliance software put it, "compliance isn't easy or cheap."[5] Basic versions of tax software may be available for low monthly fees, but substantial additional fees apply for "premium" services including support for additional jurisdictions, ready-to-file return preparation, and actual remittance of sales taxes to each taxing authority. In addition, the Petitioner and its Amici ignore the substantial cost of staff time to integrate the software into existing accounting and payment management systems, including the staff time required to identify and enter product and purchaser information for the software to work. Such work is especially burdensome for auction companies because prices in every auction for every single item are different, established on an item-by-item basis by the successful bidders. In addition, unlike a large retailer that sells thousands or perhaps millions of identical products at identical prices, products offered by auction houses are often rare or unique and there is little overlap from auction to auction. All of these variables will make compliance by auctioneers expensive and cumbersome.

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[5] *Cloud Commerce and Sales Tax Compliance*, Avalara Whitepaper, https://www1.avalara.com/us/en/learn/whitepapers/cloudcommercesalestax.html.

The *Quill* Court correctly determined that, although not a perfect standard, the physical presence requirement "foster[ed] investment by businesses and individuals" and had "become part of the basic framework of a sizable industry." *Quill*, 504 U.S. at 316-17. Significant growth of interstate commerce in the years since *Quill* makes that reasoning even stronger. Physical presence remains a straightforward, workable standard on which businesses can rely to know which state sales taxes they are responsible for collecting. As states increasingly test the limits of "physical presence," abrogating *Quill* will only exacerbate the uncertainty surrounding whether sellers must collect sales taxes, inviting endless litigation over the meaning of "substantial nexus" or "undue burden" instead of physical presence.

Finally, if this Court abrogates *Quill* states will be free to impose retroactive tax liability on businesses for prior sales. This will only compound the burdens on small businesses. Where such economic interests are at stake, this Court has recognized that *stare decisis* carries the most weight. Petitioner and its Amici have not made the compelling showing required for this Court to invalidate a 50-year precedent explicitly affirmed in 1992.

This Court should affirm the decision of the South Dakota Supreme Court and uphold the physical presence requirement this Court adopted in *Bellas Hess* and re-affirmed in *Quill*.

ARGUMENT

I. OVERRULING THE PHYSICAL PRESENCE RULE WILL ADVERSELY IMPACT AUCTIONEERS AND OTHER SMALL BUSINESSES TO THE BENEFIT OF AMAZON AND OTHER LARGE E-COMMERCE COMPANIES

Petitioner's focus on large internet retailers misses an important thread in this case: the incremental benefit to states is far outweighed by the significant damage to small businesses engaged in interstate commerce if this Court repeals *Quill*'s physical presence requirement. While Respondents may be easy targets for Petitioner and its Amici, a significant portion of interstate commerce is made up of small businesses engaged in consumer sales.[6] Unlike their larger competitors, most small businesses open up shop where they live. They do not strategically locate their operations to obtain a competitive advantage over brick-and-mortar competitors. These businesses are not clinging to an unfair tax advantage; they simply have limited resources to comply with a messy patchwork of obligations from thousands of different taxing jurisdictions. It is these small businesses that will bear the brunt of burdensome compliance in a post-*Quill* world.

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[6] *See* Donald Bruce and William F. Fox, *An Analysis of Internet Sales Taxation and the Small Seller Exemption*, University of Tennessee Center for Business and Economic Research for the Small Business Association, at 31 (Nov. 2013) (finding that almost 43% of retail e-commerce is from companies with sales of less than $1 million annually).

South Dakota claims that imposing a sales tax on businesses without a physical presence in the state is simply "leveling the playing field" between physical and on-line retailers. Ironically, while Petitioner repeatedly cites Amazon as an example of the unfairness of the physical presence requirement, Amazon now collects sales taxes in every state that imposes state sales taxes.[7] Amazon is not an outlier in this regard but representative of a broader trend among large internet retailers. According to a November 2017 report of the United States Government Accountability Office, approximately 80 percent of the potential revenue from internet retail sales is already collected or collectible under current law.[8]

In fact, the actual impact of the physical presence rule on state revenues is much smaller than Petitioner and its Amici contend. Abrogation of the physical presence rule would only increase state and local sales tax receipts by an estimated two to four percent of their 2016 totals.[9] While this is not negligible, it is hardly a constitutional crisis. In South Dakota, the additional revenue derived from the collection of sales taxes by out-of-state businesses will not be used to fund essential services in the state but to reduce

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[7] Chris Isidore, *Amazon to Start Collecting State Sales Taxes Everywhere*, CNN (Mar. 29, 2017) http://money.cnn.com/2017/03/29/technology/amazon-sales-tax/index.html.

[8] U.S. Government Accountability Office, GAO-18-114, *Sales Taxes States Could Gain Revenue from Expanded Authority, But Businesses are Likely to Experience Compliance Costs*, at 9 (Nov. 2017), https://www.gao.gov/assets/690/688437.pdf [hereinafter "U.S. GAO Report"].

[9] U.S. GAO Report, *supra* note 8, at 12.

other state taxes.[10] S.D. Codified Laws § 10-64-9 ("If the state is able to enforce the obligation to collect and remit sales tax on remote sellers . . . the additional net revenue from such obligation shall be used to reduce the rate of certain taxes."). Thus, under South Dakota law, the purported benefit of repealing the physical presence requirement for South Dakota is lower taxes for South Dakotans.[11] This benefit must be measured against the additional burden on interstate commerce if the physical presence requirement is eliminated.

Small businesses provide economic benefits to their communities and are a key component of interstate commerce. Auction companies in particular help state and local governments sell surplus property, help families liquidate estates, help businesses buy and sell highly specialized equipment, and connect individual buyers with individual sellers to facilitate

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[10] South Dakota's proposal to reduce taxes in other areas undermines the argument made in the Amicus brief filed by Colorado, et al., that the explosion of internet sales robbed state treasuries of sales tax causing huge cuts in essential state programs. This argument rests on mere correlation, providing no evidence that the shortfalls necessitating the cuts were not brought on by other cracks in the states' taxing framework, like a greying workforce, reductions in federal funding, reduced property and income taxes, and the like.

[11] The claimed reduction of South Dakotans' taxes is an illusion because it is South Dakotans who will be paying the sales taxes that are ultimately collected under South Dakota's statute. In reality, South Dakota is essentially shifting how it taxes its residents rather than seeking a lost revenue stream. States are certainly within their right to choose a method or methods of taxation to impose on their residents, but these methods are subject to constitutional limitations, including the commerce clause.

transactions that would otherwise go unrealized. They pay taxes, including sales taxes when required in the jurisdictions in which they host auctions. They rely on *Quill* as an assurance that, merely by holding an auction in one state, they will not potentially become subject to many different state and local sales tax rules.

A. If this Court Overturns *Quill*, Small Businesses Will Be Forced to Collect Sales Tax on Even Minimal Interstate Sales

South Dakota argues that its statute is appropriately structured to exempt businesses that do not have significant sales in South Dakota. Specifically, South Dakota's statute applies to businesses that do more than $100,000 in sales or more than 200 transactions per year. S.D. Codified Laws § 10-64-2. Through this claimed *de minimis* exception, South Dakota may have intended to net only whales, but its bycatch will inevitably include many minnows.

Auctions are a perfect example of how South Dakota's statute will affect small businesses. Hundreds of items may be sold in a single auction, and often a single bidder will purchase dozens or more items. Under South Dakota's statute, if a handful of South Dakota residents become winning bidders on as few as 200 items in an out-of-state auction, whether live or online, South Dakota imposes a sales tax on the auctioneer. Each of those items would then need to be analyzed for exempt status, the appropriate sales tax rates would need to be calculated and collected for each item, and the total amount would need to be filed with South Dakota's Department of Revenue. This burdensome obligation could be triggered for as little as a few thousand dollars of purchases in a single auction.

Moreover, a small business cannot know if it will exceed the exemption thresholds in any given year. Under South Dakota's law, a seller is required to pay[12] sales taxes if it exceeds one of the thresholds "in the previous year or the current calendar year." S.D. Codified Laws § 10-64-2 (emphasis added). This standard requires a business to predict ahead of time whether it will later exceed the statute's thresholds in a calendar year. As a result, small businesses will likely feel forced to collect sales taxes, even if they are unlikely to exceed the statutory thresholds, since failing to do so and later exceeding one of the thresholds would result in the business absorbing the sales tax and facing possible non-compliance fines and penalties.

For example, if a business does not expect to exceed the revenue or transaction thresholds, it may choose not to collect sales taxes from South Dakota residents. If it then has a better than expected year and exceeds one of the thresholds, it will become responsible for taxes on sales made for the entire year. Unable to collect sales taxes from customers for

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[12] The Brief for the United States proceeds from the false premise that South Dakota has imposed a mere collection requirement and not a tax on out-of-state sellers. Brief for the United States As Amicus Curiae Supporting Petitioner, at 11-23 (March 5, 2018). Under South Dakota law, however, the sales tax actually applies to the gross receipts of a business and the business is required to pay the tax regardless of whether it collects it from customers. S.D. Codified Laws § 10-45-2; South Dakota Department of Revenue, Sales and Use Tax Guide, at 3 (July 2017), https://dor.sd.gov/Taxes/Business_Taxes/Publications/PDFs/STGuide.pdf ("[T]he seller is liable for the sales tax due, whether or not it is collected.").

sales made earlier in the year, it will be forced to pay the taxes itself. To avoid this scenario, the small business needs to charge sales tax on the very first sale it makes to a South Dakota resident. In short, from a practical standpoint, South Dakota's *de minimis* exemption is illusory.

Furthermore, other states will not be bound to South Dakota's exemption levels and will be free to impose sales tax on any and all sales. While Petitioner contends that states are unlikely to ensnare small businesses in minimal collection requirements, logic and experience suggest otherwise. A constitutional standard that depends on fifty states and thousands of taxing jurisdictions working together and agreeing on a single, streamlined collection process and exemption threshold is the height of folly. (Resp't's Br. at 16-19). States already have an interest in protecting their own businesses from burdensome taxation and streamlining sales taxation collection across state lines. Despite this incentive, states have adopted a wide variety of taxation schemes to generate additional sales tax revenue from out-of-state businesses.[13]

This strategy is unsurprising. Out-of-state sellers are an attractive target for states. Unlike their in-state counterparts, out-of-state sellers, especially small businesses, often lack political influence in the taxing state. Elected officials, wary of increasing other taxes on their constituents, will eagerly pursue sales tax revenue from out-of-state sellers.

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[13] Brief of Tax Foundation as Amicus Curiae in Support of Neither Party, at 24-25 (Mar. 5, 2018) (collecting state statutes) [hereinafter "Tax Foundation Brief"].

In fact, some states have already adopted lower exemption thresholds in their expanded physical presence and reporting requirement statutes, as low as $10,000 (in 16 states), $5,000 (in Rhode Island), $2,000 (in Connecticut), and even no exemption whatsoever (in Pennsylvania).[14] These low exemption thresholds illustrate the impact on small businesses in a post-*Quill* world. As Justice Alito put it during oral argument in *Direct Marketing Association v. Brohl* (speaking only to the number of states, not the thousands of other taxing jurisdictions): "Now I will have to submit potentially 50 different forms to all of these States reporting that somebody in South Carolina purchased something from me that cost 23.99." Transcript of Record at 32:14-21, *Direct Mktg. Ass'n v. Brohl*, 575 U.S. ___, 135 S.Ct. 1124 (2015).

Petitioner and its Amici attempt to downplay the chaotic mess of state and local sales and use taxes by noting that "many" states have moved toward simplified collection processes. (Pet'r's Br. at 13). In reality, only 24 states accounting for one-third of the United States' population have joined the Streamlined Sales Tax Agreement.[15] Having a streamlined reporting procedure in a minority of states does nothing to simplify the compliance burden in the states that have not adopted such a procedure.

In fact, it is likely that some states are working together and using carrots to incentivize compliance precisely because of *Quill*. If *Quill* is overruled, states will not need carrots to induce compliance; they will

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[14] Tax Foundation Brief, *supra* note 13, at 20-25.

[15] U.S. GAO Report, *supra* note 8, at 18.

have more effective sticks: the state's enforcement powers. Letters offering compliance assistance and reduced price software will quickly turn into demand letters, audits, and threats of litigation. States rarely offer compliance assistance and free software for their in-state businesses. It is unlikely they would do so for out-of-state businesses.

Under our constitutional government the only entity that can harmonize these inconsistent demands on interstate commerce is Congress. As this Court observed in *Quill*, Congress has the authority under the commerce clause to overturn the physical presence requirement. *Quill*, 504 U.S. at 318. Only Congress can ensure that the burden of inconsistent state and local sales tax regimes does not stifle interstate commerce by standardizing state sales tax collection and providing adequate and uniform exemptions for small businesses.

B. Contrary to Petitioner's Arguments, Complying with Different State and Local Tax Regimes Will Substantially Burden Small Businesses

As noted above, auction companies are small businesses, with 94% of NAA members having fewer than twenty employees and more than 80% having fewer than ten.[16] Businesses this size often operate on small margins. Most lack both the in-house expertise for multi-jurisdiction tax compliance and the resources to hire new staff to handle compliance issues. Like many small businesses, most auction companies have a bookkeeper or office manager or family member with

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[16] NAA Membership Database (March 12, 2018).

a variety of job responsibilities handling state tax returns rather than a full-time accountant.

The cost of hiring new staff or outside experts to comply with expanded sales tax collection requirements is prohibitive for such small businesses. According to the Aberdeen Group, the average cost of employees dedicated to sales and use tax management is already over $63,000 per year for small businesses.[17] This will only increase if this Court abrogates *Quill*. Engaging outside accountants and tax attorneys for tax compliance assistance will be infeasible for the majority of small businesses including auctioneers.

As Petitioner and its Amici appear to acknowledge (Pet'r's Br. at 46), tax compliance software is the only realistic way to comply with the quagmire of inconsistent state and local sales tax rules. As an initial matter, this Court should be highly skeptical of the claim that an extremely complex service like multi-jurisdiction sales tax compliance is being offered by private companies for little or no cost. Much of the data cited by Petitioner comes from these tax compliance providers themselves. Obviously, these companies have a clear financial interest in making their products appear reasonably priced for potential clients. Tax compliance companies hire teams of tax attorneys and other professionals who constantly monitor changes in each of the more than 10,000 taxing jurisdictions in the country. The notion that these for-profit companies will essentially give away a

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[17] Nick Castellina, *The Roadmap to Sales and Use Tax Compliance*, Aberdeen Group (Mar. 30, 2016), http://www.aberdeenessentials.com/cfo-essentials/the-roadmap-to-sales-and-use-tax-compliance/.

product that requires such extensive manpower and expertise is patently false.

While the costs to license tax compliance software may start at tens of dollars per month for a limited number of sales and taxing jurisdictions, unlimited access can cost up to $200,000 per year in licensing fees alone.[18] These costs are only for basic service. To access "premium" options, businesses must pay much higher monthly fees. These premium options include tasks such as providing ready-to-file returns and actually remitting sales taxes to the appropriate taxing authorities. If this court eliminates the physical presence rule, it is likely that surging demand would further drive up prices for software.

One NAA member company investigated the cost of tax compliance software in 2017. In that year, this auction company sold 92,105 lots[19] at auction across 12,078 invoices and remitted a total of $856,051 in sales tax to approximately 200 different taxing jurisdictions based on the location of the seller's assets.[20] For this company, the licensing cost for basic service was quoted as $945 per year plus $45 per return filed. Since many states require monthly filings, the cost to this company for filing returns was expected to be more than $2,200 per month. Thus, the total software cost was estimated to be approximately $25,000

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[18] U.S. GAO Report, *supra* note 8, at 19.

[19] A "lot" is an article or articles offered as one item in an auction. Definition of Lot, Merriam-Webster, https://www.merriam-webster.com/dictionary/lot.

[20] These sales taxes are based on the total value of the sale, not the minimal commission the auction house made on each sale.

per year for this one auction company under current law. While these prices may no longer be current, this example demonstrates how software costs can be much higher than they initially appear.[21] If the physical presence rule is overturned, this company's software licensing costs would be significantly greater. Instead of applying sales tax based on the location of the seller's assets at each auction, the auction company would be required to look up and calculate sales tax based on where the buyer receives the purchased items, for over 12,000 invoices in the cited example. This would greatly increase the required number of tax returns and corresponding software fees.

Moreover, software fees are just the tip of the iceberg. Once purchased, the software must be integrated into a business's current payment processing and accounting systems. The type of seamless integration described by the National Association of Certified Service Providers[22] is generally limited to integration with a business's online shopping cart system. As the U.S. GAO Report found, "[b]usinesses would either have to incur additional costs to better integrate sales tax software with existing business

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21 *See* Larry Kavanagh and Al Bessin, *The Real-World Challenges In Collecting Multi-State Sales Tax*, TruST, at 3 (Sept. 2013), http://truesimplification.org/wp-content/uploads/Final_TruST-COI-Paper-.pdf (estimating annual software fees for mid-market retailers at between $25,000 to $50,000 annually) [hereinafter "Kavanagh Report"].

22 Brief of the National Association of Certified Service Providers and the Software & Information Industry Association as Amicus Curiae in Support of Neither Party, at 6 (Mar. 5, 2018).

information systems (such as general ledger accounting system), or regularly reconcile receipts and records manually to prepare sales tax returns for all states where it makes sense."[23] If a business uses custom or uncommon software, integration of the tax software into its operations will be even more expensive and future software changes will be limited to compatible products and require additional integration costs. Businesses may therefore feel "locked in" to a specific provider, unable to switch if they are unhappy with their products or service.

After the software is integrated into a business's existing systems, the tax compliance software is only as good as the information uploaded to it. Much of the compliance burden on businesses will be entering product information into the software, a process known as mapping. Mapping requires the coding of all of a business's products to the specific taxation categories listed in the software. This allows the software to determine whether the item is subject to sales tax in a given jurisdiction and the applicable tax rate. Product mapping must be done "with sufficient precision for the software to assign its tax status based on state laws."[24]

Because state and local tax rules are so varied, mapping requires a substantial amount of staff time and product knowledge to ensure that each product is correctly identified and categorized in the software. Otherwise, taxes may be collected on products that are exempt or vice versa. In the auction business, such

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[23] U.S. GAO Report, *supra* note 8, at 19-20.

[24] U.S. GAO Report, *supra* note 8, at 17.

product mapping presents an enormous challenge, both because goods sold at auction are often unique or used items and because of the state-by-state differences in what is or is not subject to sales taxation. For example, farm equipment is generally subject to sales tax in South Dakota but there are exemptions for equipment used to raise certain types of animals and other agricultural products.[25] In Minnesota, farm equipment is generally exempt from sales tax, but the exemption does not apply to certain specific categories of equipment, including equipment used to raise horses and equipment used on hobby farms.[26] Thus, to complete the mapping process for farm equipment correctly, an auctioneer seller must enter detailed information about the product, including: (1) whether the product is farm equipment; (2) whether it is used for commercial purposes or hobby farming; (3) whether the equipment is used to raise animals; and, if so, (4) which specific animal or animals. This is only one example. Other states may apply taxes to new equipment but not used, apply different rates to different types of products, or apply finer distinctions between the type or volume of farm goods and equipment sold.[27] And this example does not even consider local sales tax rules.

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[25] South Dakota Department of Revenue, Farmers and Use Tax (July 2017), https://dor.sd.gov/Taxes/Business_Taxes/Publications/PDFs/Tax%20Facts/Farmers%20Use%20Tax.pdf.

[26] Minnesota Department of Revenue, Sales Tax Fact Sheet 106, Farm Machinery (Aug. 2016), http://www.revenue.state.mn.us/businesses/sut/factsheets/fs106.pdf.

[27] South Dakota Department of Revenue, Agricultural Products (July 2017), https://dor.sd.gov/Taxes/Business_Taxes/Publications/

Examples like this are common in the auction industry. One online auction platform that specializes in construction and agricultural equipment reported 2017 sales of more than $623 million, from more than 2,600 sellers.[28] This online platform allows qualified auctioneers to sell to registered bidders that are in the market for specialized equipment. Through platforms like these, small auction companies can reach a much wider audience, which is critical for selling these types of highly specialized equipment at auction. The result is good for both sellers who see more revenue and buyers who have access to more products, but such specialized equipment is often subject to detailed tax rules that vary widely state.

Auction companies that do not sell specialized industrial or agricultural equipment will also be heavily burdened by the mapping process. These companies sell a large and varied number of items at prices that are different and unknown until the sale is completed. Some states, including South Dakota, even have specific taxation rules that apply only to auctions,[29]

PDFs/Tax%20Facts/Ag%20Products.pdf (medicine for animals is subject to sales tax unless it is mixed with feed prior to being sold; commercial fertilizers are exempt if greater than 500 pounds per case; bedding for exempt animals is exempt but the exemption only applies to straw, corn stover, and bean straw).

28 *AuctionTime.com Reports Over $623 Million In Equipment Sold In 2017*, OpenSource Magazine (Jan. 4, 2018), http://opensource.sys-con.com/node/4216044.

29 *See, e.g.*, South Dakota Department of Revenue, Auctioneers, Auction Clerks and Auction Services (July 2013), https://dor.sd.gov/Taxes/Business_Taxes/Publications/PDFs/auctions0713.pdf; Minnesota Department of Revenue, Sales Tax Fact Sheet 132, Isolated and Occasional Sales (Aug. 2017), http://www.revenue.

likely requiring both higher licensing fees for specialized tax software and greater effort to complete the mapping process. Unlike other businesses in which mapping will be most burdensome in the initial start-up phase, this expensive, time-consuming burden will be ongoing for auction companies because the specific items sold at each auction are different and the sale prices are unknown until the bidding closes.

Integration and mapping are mere precursors to collecting and remitting sales taxes. Businesses must collect and account for all sales tax collections, prepare tax returns for each state and local jurisdiction where they have qualifying sales, and remit payment to the appropriate taxing authority. The process of sales tax remittance varies greatly by state. Many states require monthly filings, others accept quarterly filings, and filing obligations may vary by sales volume.[30] South Dakota requires businesses to file a return for each reporting period, regardless of whether they made any sales during that period.[31] Each business will need to register and obtain a license from

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state.mn.us/businesses/sut/factsheets/fs132.pdf; Illinois Department of Revenue, Sales Tax Issues for Auctioneers (April 1991), http://www.revenue.state.il.us/publications/bulletins/1991/FY91-49.PDF.

30 *See, e.g.*, New York State Department of Taxation and Finance, TB-ST-275, Filing Requirements for Sales and Use Tax Returns (November 20, 2015), https://www.tax.ny.gov/pdf/tg_bulletins/sales/b15_275s.pdf.

31 South Dakota Department of Revenue Sales and Use Tax Guide, at 11 (July 2017), https://dor.sd.gov/Taxes/Business_Taxes/Publications/PDFs/STGuide.pdf ("Your business must file a tax return each reporting period even if you did not conduct business or receive income.").

applicable taxing jurisdictions, some of which require a registration fee,[32] and all of which require additional time and paperwork. Only after all of these resources in both time and money are expended can the business collect and remit sales taxes for out-of-state sales.

Remitting sales taxes does not mark the end of the compliance burden. Many small businesses will face even greater compliance costs in the form of assessments and audits from state and local taxing authorities. Unlike many large businesses, which often have entire compliance departments, small businesses are forced to do the best they can with limited resources. Indeed, the U.S. GAO Report found reason to believe small and medium-sized businesses will be audited because such audits often generate additional state revenue.[33] Audits can be extremely expensive and time consuming for even large businesses and outright disastrous for small ones. [34]

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[32] Jennifer Dunn, *Which States Charge a Fee to Register for a Sales Tax Permit*, TaxJar (June 14, 2016), https://blog.taxjar.com/fee-register-for-a-sales-tax-permit/.

[33] U.S. GAO Report, *supra* note 8, at 21.

[34] In one example, an auctioneer without a physical presence in South Dakota opted to surrender its South Dakota sales tax permit due to limited sales in South Dakota. Thereafter, if the auctioneer held an auction in South Dakota it remitted the sales taxes. In 2015, South Dakota demanded that the auctioneer reacquire a sales tax number and within 60 days of it doing so, South Dakota issued a notice of Sales Tax Audit in which it demanded records for every auction for the previous three to five years regardless of its location. The audit took three weeks, disrupting the auctioneer's office and business, as auditors looked

Even if the risk of an audit is low, state taxing authorities have other enforcement tools, such as assessment letters. These letters are mailed to businesses that the state believes may owe sales taxes. The burden is then on each business to prove that the taxing authority is wrong. Small businesses are unlikely to have the wherewithal to challenge a state's assessment, even when they have good reason to conclude that it is incorrect. Challenging an incorrect assessment may require hiring counsel and accountants in the taxing state and traveling to the state to appear before the taxing authority. At a minimum, it will require staff time to investigate and respond to the assessment letter.

If an out-of-state business decides to challenge a state's assessment or tax law, it will be forced to litigate the issue in state court in the taxing state. Under the Tax Injunction Act, federal district courts may not entertain a challenge to the "assessment, levy or collection" of a state tax if there is an acceptable remedy in state court. 28 U.S.C. § 1341. Thus, not only will a business with little connection to a taxing state be forced to litigate in that state, it will be forced to do so in a forum that may be inherently biased in favor of the state's tax collectors. *See Roberts v. Mars Petcare US, Inc.*, 874 F.3d 953, 956 (6th Cir. 2017) (explaining purpose of diversity jurisdiction is to "protect out-of-state parties from the potential risk that local juries (or judges) would favor in-state parties").

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for any transaction involving a South Dakota resident. This audit has become an annual event.

While there are ways to minimize the compliance burden on small businesses,[35] they require uniform, voluntary action from all states (which has not yet happened and is unlikely ever to occur). Absent voluntary action by all states, only Congress can mitigate or eliminate the burdens on interstate commerce that would result from the repeal of the physical presence requirement. Congress would be able to guarantee meaningful small business exemptions, guarantee simplified reporting requirements, or even require compensation for compliance. Without such Congressional action, the physical presence requirement is the only bulwark protecting small businesses from a burdensome deluge of tax collection requirements.

II. OVERTURNING THE PHYSICAL PRESENCE RULE ANNOUNCED IN *BELLAS HESS* AND AFFIRMED IN *QUILL* WOULD BE CONTRARY TO *STARE DECISIS* AND UPSET THE SETTLED EXPECTATIONS OF ENTIRE INDUSTRIES

The physical presence rule, announced in two of this Court's decisions, has been the law of the land for over 50 years. Abrogating the rule will create immediate compliance concerns for thousands of businesses that rely on this standard and could subject many of them to retroactive liability for prior sales. Given these considerations, there are likely few cases in which *stare decisis* should carry more weight.

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35 *See, e.g.*, David Gamage and Devin J. Heckman, *A Better Way Forward for State Taxation of E-Commerce*, 92 B.U. L. Rev. 483 (2012), https://scholarship.law.berkeley.edu/cgi/viewcontent.cgi?article=2700&context=facpubs (arguing that states should compensate businesses without a physical presence for their costs to comply with sales tax collection requirements).

Petitioner's arguments are virtually identical to the arguments this Court rejected in *Quill*. The Court specifically noted the incredible growth and size of the mail-order industry, to an extent that could not have been imaginable at the time *Bellas Hess* was decided. Although Petitioner attempts to downplay the size and importance of the mail order industry when *Quill* was decided, at that time the North Dakota Supreme Court described the industry as a "'goliath' with annual sales that reached 'the staggering figure of $183.3 billion in 1989.'" *Quill*, 504 U.S. at 303. This was not some unimportant, fledgling industry but a massive part of the economy, generating over $360 billion in sales in today's dollars.[36] This is actually more than all business-to-consumer internet retail sales from the top 1,000 internet retailers in 2017.[37]

The *Quill* Court even considered the centerpiece of Petitioner's argument that "advances in computer technology greatly eased the burden of compliance with a 'welter of complicated obligations' imposed by state and local taxing authorities." *Id.* at 303. Since *Quill* was decided, the number of state and local sales tax jurisdictions has only increased and the rules have become even more complex.[38] The fact that businesses can pay for expensive tax compliance software is not a sufficient reason for this Court to overturn the physical presence standard. As explained above,

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[36] U.S. Inflation Rate, 1989-2017 ($183,000,000,000), http://www.in2013dollars.com/1989-dollars-in-2017?amount=183000000000.

[37] U.S. GAO Report, *supra* note 8, at 9.

[38] Tax Foundation Brief, *supra* note 13, at 13.

software costs are only one portion of the burden that will result if the physical presence requirement is eliminated.

A. Auction Companies and Similar Small Businesses Have Relied on the *Quill* Rule for Decades

This Court approaches "with the utmost caution" reconsideration of any of its decisions, and "[c]onsiderations in favor of *stare decisis* are at their acme in cases involving property and contract rights, where reliance interests are involved. . . ." *Pearson v. Callahan*, 555 U.S. 223, 233 (2009). None of this Court's justifications for overturning its precedent are present in this case. Overturning the physical presence requirement will upset settled expectations; the physical presence requirement is not a "recently adopted" judge-made rule; and, although this is not a case of statutory construction, "Congress is free to change this Court's" decision at any time. *Id.*; *see Payne v. Tennessee*, 501 U.S. 808, 828 (1991) (explaining rationale for applying lower threshold for *stare decisis* in constitutional cases is because "correction through legislative action is practically impossible"). Even if this Court concludes that *Quill* is wrong, it should nevertheless uphold the physical presence rule because "it is more important that the applicable rule of law be settled than it be settled right." *Payne*, 501 U.S. at 827. This wise sentiment is particularly true in this case in which entire industries have grown in reliance on the physical presence requirement.

One obvious inequity that would result if this Court abrogates *Quill* is that it will effectively punish sellers in states that do not have a sales tax. Five

states—Alaska, Delaware, Montana, New Hampshire, and Oregon—have no state sales tax.[39] Small businesses in these states have no experience with collecting sales tax for either online or in-person sales. The physical presence rule shields these businesses from having to spend resources complying solely with other states' sales tax laws. Without *Quill*, these businesses will face higher costs of compliance simply because they happen to be located in a state without a sales tax.[40] The idea that South Dakota could adopt a tax that Oregon has rejected and subject Oregon's businesses to onerous tax collection requirements is exactly the type of extra-territorial reach that this Court's long-standing precedent seeks to prevent. *See Miller Bros. Co. v. Maryland*, 347 U.S. 340, 342 (1954) ("If the legislature of a State should enact that the citizens or property of another State or country should be taxed in the same manner as the persons and property within its own limits and subject to its authority, or in any other manner whatsoever, such a law would be as much a nullity as if in conflict with the most explicit constitutional inhibition.").

In addition to the inequities wrought upon sellers in certain states, some types of business will suffer more than others. Many businesses across the country have adjusted their sales strategies in reliance on *Quill*. Many remote sellers have business models that

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[39] Jared Walczak and Scott Drenkard, *State and Local Sales Tax Rates in 2018*, Tax Foundation (Feb. 13, 2018), https://taxfoundation.org/state-and-local-sales-tax-rates-2018/. Many municipalities in Alaska have a local sales tax.

[40] U.S. GAO Report, *supra* note 8, at 20.

emphasize low margins and high sales volume.[41] Auction companies have embraced marketing strategies that target regional and national audiences. These businesses may not be able to absorb the additional burden of multi-jurisdiction tax compliance.[42] It would be extremely unfair for businesses that relied on *Quill* to expand into new markets or develop their business strategies to find themselves suddenly subject to sales tax collection requirements in possibly thousands of taxing jurisdictions.

One of the great benefits of the physical presence requirement in the modern economy is that it minimizes barriers to entry for new businesses. Anyone can create a business and sell products to individuals anywhere in the country without becoming subject to each state's tax rules. Auction companies are a perfect example of the type of dynamism that results from the "demarcation of a discrete realm of commercial activity that is free from interstate taxation." *Quill*, 504 U.S. at 315. Auctioneers increase economic efficiency by connecting willing buyers with willing sellers, facilitating sales that would not otherwise occur. Not only auction companies, but also the many other businesses that depend on auctions to sell or purchase important equipment, will suffer alike from abrogation of the physical presence rule.

The impact will not be limited to the auction industry. Smaller firms throughout the economy will struggle to expand into new markets since doing so will trigger onerous filing obligations. Such burdens

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41 U.S. GAO Report, *supra* note 8, at 26.

42 Kavanagh Report, *supra* note 21, at 8.

will inure to the benefit of retail giants and large e-commerce companies that have grown under the protection of the physical presence requirement and now have the resources to survive in a post-*Quill* environment. Smaller competitors already disadvantaged by a company like Amazon's overwhelming economies of scale will be further disadvantaged by the sudden imposition of additional costs, in both time and money, spread over far fewer employees.[43] Thus, far from correcting an inequity, overturning the physical presence rule will create one.

B. The Physical Presence Rule Provides Clarity; Overturning It Would Invite Greater Uncertainty and Further Litigation

Petitioner and its Amici argue that *Quill*'s physical presence rule has become unworkable. They pose a series of seemingly difficult questions about how the physical presence rule is becoming more difficult to apply in the lower courts. (Pet'r's Br. at 31). Many of these scenarios have, however, already been answered, *Quill*, 504 U.S. at 315 n.8 ("Quill's licensing of software in this case does not meet the 'substantial nexus' requirement of the Commerce Clause."); *Nat'l Geographic Soc'y v. Cal. Bd. of Equalization*, 430 U.S. 551, 556 (1977) (rejecting "slightest presence" standard for finding of substantial nexus), and the remaining questions are answerable.[44] To the extent these cases

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[43] Kavanagh Report, *supra* note 21, at 7 ("Small to mid-market online and catalog merchants end up with virtually the same complexity without nearly the same revenue to cover the cost.").

[44] *See* Arthur R. Rosen and Richard C. Call, *What is Minimal Substantial Nexus?*, State Tax Notes, Vol. 85 No. 1, at 57-58

will be litigated, they present primarily legal questions that can be resolved through motion practice without the time and expense of preparing an extensive record. *Cf. Bibb v. Navajo Freight Lines, Inc.*, 359 U.S. 520, 526-28 (1959) (summarizing extensive evidence demonstrating that a nondiscriminatory regulation constituted a burden on interstate commerce). For small businesses, *Quill*'s bright line rule remains just as bright today.

At a more fundamental level, the fact that a constitutional tenet must be applied to modern technology is not a reasonable basis to abandon it wholesale. As with any constitutional rule, new technology requires courts to consider how to apply old doctrines. This Court's dormant commerce clause jurisprudence previously protected interstate sales via fax, phone, and common carrier; it now extends to sales through the internet. This is neither surprising nor a valid basis to abandon precedent.

Even if this Court agrees that the physical presence requirement is becoming increasingly difficult to apply, abrogating *Quill* will not add clarity to the "quagmire" of dormant commerce clause jurisprudence. To the contrary, it will open the door to more confusion and endless litigation. Instead of determining whether a business has a physical presence in a state (which despite Petitioner's examples of a few tricky cases remains a very straightforward analysis), lower courts will have to determine on a case-by-case basis whether a business has a "substantial nexus" to the taxing

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(July 3, 2017), https://www.mwe.com/~/media/files/press-room/2017/07/rosencall-7317.pdf?la=eng (arguing for specific nexus requirement under physical presence rule).

state, or, even worse, whether the tax represents an "undue burden" on interstate commerce.

In *Complete Auto Transit, Inc. v. Brady*, this Court adopted a four-part test for evaluating state taxes under the commerce clause: (1) the tax must apply to an activity with a substantial nexus with the taxing state, (2) it must be fairly apportioned, (3) it must not discriminate against interstate commerce, and (4) it must be fairly related to the services provided by the state. 430 U.S. 274, 279 (1977). *Bellas Hess* and *Quill* address the first prong of the test: whether the activity has a substantial nexus with the taxing state. *Quill*, 504 U.S. at 311. Without the physical presence requirement as a bright line test, lower courts will struggle to define when a state can constitutionally impose a sales tax on an out-of-state business.

Would a finding of substantial nexus be based purely on the value of goods sold in the taxing state? If so, what is the threshold value and how will it be adjusted over time? Should it differ depending on the size of the state? Is the number of transactions relevant to a finding of substantial nexus? Would a business's marketing activity or lack thereof in the taxing state affect the analysis?[45] If South Dakota's law defines the parameters of the constitutional substantial nexus standard, 200 transactions at $10 per item would result

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[45] *See* Joseph Bishop-Henchman, *Why the Quill Physical Presence Rule Shouldn't Go the Way of Personal Jurisdiction*, Tax Foundation (Nov. 5, 2007), https://taxfoundation.org/why-quill-physical-presence-rule-shouldnt-go-way-personal-jurisdiction/ (raising concerns about the workability of an economic nexus standard).

in a finding of substantial nexus with only $2,000 of sales, but one sale of a luxury item for $90,000 would be insufficient nexus regardless of the marketing activity of the business. This is true even though the revenue at stake in the latter case is 45 times greater and even though it would be much simpler for the seller of a single expensive item to collect and remit sales tax to the state.

Several Amici argue that the Court should not apply the *Complete Auto* test at all, arguing instead for the Court to adopt the undue burden or *Pike* test, which is generally applied to regulations that have an incidental impact on interstate commerce. Under the test set forth in *Pike v. Bruce Church, Inc.*, an even-handed statute that furthers a legitimate state policy "will be upheld unless the burden imposed on such commerce is clearly excessive in relation to the putative local benefits." 397 U.S. 137, 142 (1970). Under this test, however, a statute might be found to be facially valid but unconstitutional as applied to specific parties. *Id.* at 143-44. It is thus conceivable that a sales tax collection requirement would present an unconstitutional burden for some businesses but not for others. Similar to the substantial nexus test, there are no obvious constitutional lines to provide much-needed certainty for businesses. Moreover, this test fails to account for the cumulative nature of different state and local tax rules, the combination of which creates a substantial burden on interstate commerce.

To make matters worse, some states, including South Dakota, impose a sales tax on services. *See* S.D. Codified Laws § 10-45-5.2. South Dakota's tax

on out-of-state businesses applies to both sales of tangible personal property and "services delivered into South Dakota." *Id.* § 10-64-2. If a business were to purchase from an out-of-state vendor consulting services that are performed entirely out of state but provided to a South Dakota resident, would that constitute sufficient nexus to require the consulting firm to collect and remit sales taxes? Many service-oriented businesses are not accustomed to collecting sales taxes, as professional services have traditionally not been subject to sales tax in most states.[46] The prospect of service taxes will make South Dakota's statute and similar state statutes that much more burdensome and difficult to apply.

If the *Quill* decision is incorrect or problematic, Congress has the power to alter the decision to ease or eliminate compliance burdens associated with such a significant rule change. *Quill*, 504 U.S. at 318. Congress can stop litigation in this area by clarifying the meaning of physical presence, clarifying the substantial nexus test, or adopting new requirements for state sales tax authority. Without Congressional action, the law will continue to develop on a case-by-case basis and each state law will contain different tests for nexus and different exemptions.

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46 David Brunori, *Don't Be Fooled – Services Should Be Subject to Sales Tax*, Forbes (Sept. 24, 2015), https://www.forbes.com/sites/taxanalysts/2015/09/24/dont-be-fooled-services-should-be-subject-to-sales-tax/#3c17d03450e7 ("Most services aren't subject to sales tax in most states.").

C. Overturning *Quill* Would Invite Retroactive State Tax Collection That Would Create Chaos for Small Businesses

In *Harper v. Virginia Department of Taxation*, a tax case, this Court was very clear that its decisions "must be given full retroactive effect in all cases still open on direct review and as to all events, regardless of whether such events predate or postdate our announcement of the rule." 509 U.S. 86, 97 (1993). Thus, if this Court were to overturn *Quill*'s physical presence requirement, that decision would have immediate retroactive application. This would allow states that already have laws on the books that tax remote sales to assess businesses for prior sales made when the physical presence requirement was the law.

Furthermore, states are not limited to existing laws; they would likely be able to pass new laws with retroactive application specifically to collect sales taxes from out-of-state businesses for prior sales. In *United States v. Carlton*, another tax case, this Court affirmed that the retroactive application of an act of Congress was consistent with principles of due process. 512 U.S. 26, 32 (1994). This Court adopted a simple test for retroactive legislation: "provided that the retroactive application of a statute is supported by a legitimate legislative purpose furthered by rational means" it will be upheld. *Id.* at 30-31. As Justice Scalia observed, the Court's test "guarantees that all retroactive tax laws will henceforth be valid" since "[r]evenue raising is certainly a legitimate legislative purpose." *Id.* at 40 (Scalia, J., concurring). The Court noted that taxation is not a penalty or a contractual liability and, accordingly, specific and detrimental

reliance on a tax rule was "insufficient to establish a constitutional violation." *Id.* at 33. Thus, there will be no constitutional prohibition on state suits against out-of-state businesses for prior years' sales taxes.

Petitioner does not contest this point but argues that states are unlikely to pursue retroactive enforcement. (Pet'r's Br. at II. D). It essentially asks this Court to trust that the states will be fair and reasonable. The increasing use of "hardball tactic[s]" to collect state sales taxes belies such trust.[47] If states are as desperate for additional revenues as Petitioner and its Amici contend, they will look to any and all sources, especially out-of-state businesses. Even if only a handful of states initially seek such back taxes, other states will then have an incentive to respond in kind with their own reciprocal measures.

Such retroactive application of new tax rules to auctioneers and other small businesses will have devastating consequences. It will not be practical and perhaps not even legal for a business to collect sales taxes from customers for prior sales. As a result, the companies themselves would be liable for back taxes, having failed to collect the tax from purchasers at the time of sale.

These "thorny questions" of retroactive sales tax liability are "better resolved by Congress rather than this Court." *Quill*, 504 U.S. at 318 n.10. If it wishes to repeal or modify the physical presence rule,

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47 Diane Yetter, *What Online Retail Clients Can Expect in the Near Future*, AccountingWeb (Mar. 15, 2018), https://www.accountingweb.com/tax/sales-tax/what-online-retail-clients-can-expect-in-the-near-future.

Congress has the authority to do so only for prospective sales, thereby protecting the reasonable expectations of thousands of businesses and fairly allocating sales tax burdens going forward. As this Court itself observed in *Quill*, "it may be that the better part of both wisdom and valor is to respect the judgment of the other branches of the Government." *Id.* at 318-19 (internal quotation marks omitted).

CONCLUSION

Twenty-five years ago, North Dakota argued that times had changed. It argued that the physical presence requirement was an anachronism due to advances in compliance software and the explosive growth of a new industry facilitating interstate commerce on a massive scale. Today, South Dakota advances the same arguments. Sometimes the more things change, the more they stay the same. The technology that facilitates interstate commerce has changed, but the physical presence rule remains just as important for small businesses, like auctioneers, that benefit from the certainty and simplicity provided by a bright line standard. This Court should continue to protect these small businesses by affirming the decision of the South Dakota Supreme Court.

Respectfully submitted,

JONATHAN M. DUNITZ
COUNSEL OF RECORD
DAVID E. WARREN
BRIAN T. MARSHALL
VERRILL DANA, LLP
ONE PORTLAND SQUARE
PORTLAND, ME 04101
(207) 774-4000
JDUNITZ@VERRILLDANA.COM

COUNSEL FOR AMICUS CURIAE

APRIL 4, 2018

APPENDIX:
LIST OF STATE AUCTIONEER ASSOCIATIONS

1. Alabama Auctioneers Association
2. Arkansas Auctioneers Association
3. Colorado Auctioneers Association
4. Florida Auctioneers Association
5. Georgia Auctioneers Association
6. Idaho Association of Professional Auctioneers
7. Illinois State Auctioneers Association
8. Indiana Auctioneers Association
9. Iowa Auctioneers Association
10. Kansas Auctioneers Association
11. Kentucky Auctioneers Association
12. Louisiana Auctioneers Association
13. Maine Auctioneers Association
14. Auctioneers Association of Maryland
15. Massachusetts Auctioneers Association
16. Michigan Auctioneers Association
17. Minnesota State Auctioneers Association
18. Mississippi Auctioneers Association
19. Missouri Professional Auctioneers Association
20. Montana Auctioneers Association
21. Nebraska Auctioneers Association
22. New Hampshire Auctioneers Association
23. New Jersey State Society of Auctioneers

24. New York State Auctioneers Association
25. Auctioneers Association of North Carolina
26. North Dakota Auctioneers Association
27. Ohio Auctioneers Association
28. Oklahoma State Auctioneers Association
29. Pennsylvania Auctioneers Association
30. South Carolina Auctioneers Association
31. South Dakota Auctioneers Association
32. Tennessee Auctioneers Association
33. Texas Auctioneers Association
34. Virginia Auctioneers Association
35. Washington Auctioneers Association
36. West Virginia Auctioneers Association
37. Wisconsin Auctioneers Association
38. Wyoming Auctioneers Association